

How to Spot an Investment Scam



In today's complex financial world, there are many investment opportunities awaiting you. As an investor, your task is to sort out those investments that have the greatest potential while still meeting your personal investment goals. As a potential investor, you may well find yourself solicited by telephone calls, mailings, and door-to-door salespersons. The majority of investment scams start on the telephone. Be prepared to deal with investment scam artists.

Indicators that the caller could be a crook

The promise of spectacular profits. The old adage is usually correct: "An offer that sounds too good to be true, probably is too good to be true."

High-pressure sales tactics.

Insistence on an immediate decision. The caller may even have a courier driving in your area ready to stop by your home and pick up your check within minutes of the call!

A "guaranteed" investment or an investment without risks.

Recommendations based on rumors, tips, inside information, or an unannounced breakthrough in the industry.

Recommendations based on the caller's ability to predict future events.

A request for your credit card number for any purpose other than to make a purchase. Requests are typically made for "identification" or "verification" purposes, or merely as an "expression of good faith."

Unwillingness to provide written information, state securities registrations, or verifiable references.

A suggestion that you invest based on trust.

Investment opportunities in another country or that are dependent on the participation of an offshore bank.

Unwillingness to let you discuss the investment with a third person.

The Most Common Areas of Investment Scams

Boiler Rooms

Often the source of the call you receive late in the evening that offers immediate investments in "get rich quick" schemes, boiler rooms earn their name from the "heat" and high pressure generated by the callers as they try to convince investors to part with their money.

Boiler rooms often are just a short-term rented apartment or office with multiple telephone lines and an impressive sounding address.

In most cases, either the company or the product does not really exist, or it does not operate as represented. Telephone pitches are read from prepared scripts with the answers to the most common objections. Your telephone number may have been obtained from

telephone directories, purchased lists, and newspaper articles. Boiler-room operators have been known to call recent widows and widowers or people who have lost large sums of money, offering to “help” recover the losses quickly and effortlessly.

Pyramid Promotions

Pyramid promotions focus on the quick profits to be earned from recruiting other investors, who then will recruit others, and so on. Little mention or emphasis is placed on the product or service to be sold. The fraud derives from the ever-decreasing number of potential investors in a given area. The common elements of a pyramid scheme involve the following:

- ✍ An invitation from a friend, neighbor, or a co-worker to attend an “opportunity meeting” to learn how to earn lots of money;
- ✍ At the meeting, a well-rehearsed presentation will downplay the traditional methods of acquiring money and will offer instead an exciting shortcut to wealth and adventure;
- ✍ Investors pay large fees for products, courses, etc., and/or the right to recruit others and profit from their participation;
- ✍ The emphasis is to get others to invest.

Pyramid schemes are illegal in Hawaii, but are difficult to prosecute. A victim’s money is often filtered up through the pyramid and lost.

Advance-Fee Loans

These loans are usually offered to desperate borrowers who have exhausted all of the traditional approaches to financing. Loans are arranged and promised only upon payment of an “up-front” or

“advance fee.” It is common for the promoter to represent the source of the funds as foreign investors or an offshore bank. Loan amount are typically very large (\$5 to \$100 million), and offer long repayment terms at below-market rates of interest. Minimal qualifications, other than the advance fee payment, are required. The promoter takes the advance fee and never delivers the loan.

Ponzi Schemes

Promoters offer high rates of return on the various impressive-sounding investments. However, instead of using the money as promised, new investor’s money is used to pay the monthly “interest” or “return” to earlier investors. These “satisfied investors” then report the high return to their friends, who in turn invest in hopes of achieving the same above-average returns.

In a Ponzi scheme, there is no underlying business. Early investors are simply being paid with the funds received from later investors. The scheme only continues as long as new investors provide additional funds. When the scheme collapses (as it always does), current investors lose their money and the promoters walk away rich.

Loan Roll Programs/Prime Bank Notes

These investments are similar in many respects to the advance-fee loan schemes described above. Promoters offer the “little guy” a chance to pool money with other investors to buy bank notes internationally, often touting a large offshore bank as instrumental in the deal.

Investments range from a few thousand dollars to a hundred thousand dollars or more. Returns of fantastic wealth are promised, often in the \$100 million range. Details about how the program works are either unavailable or, when examined closely, nonsensical.

Gold and Silver Mines

These speculative investments typically offer new or secret methods for reclaiming mineral reserves from untested or abandoned mines, or even the recovery of microscopic traces of valuable minerals from soil in your geographic area “where no one else would think to look!” These are classic frauds. Often, the promoter will base a mining forecast on an unknown expert’s geological report or prediction, or will offer part of a valid report out of context. Promoters exaggerate the quality and quantity of the minerals to be extracted, while downplaying the expense or likelihood of recovering them.

Oil Wells

By acquiring interest in a “proven” oil field or in the immediate vicinity of other proven oil fields, investors are promised “can’t-miss opportunities” for great wealth. These investments are frequently sold to people who live far from the oil company’s headquarters, which may be nothing more than a rented trailer.

As with gold and silver mines, promoters frequently offer new and secret methods for reclaiming missed oil reserves on previously drilled oil fields.

Coins and Precious Metals Schemes

Promoters offer “investment grade” gold and silver coins, claiming their present value can be independently verified and promising tremendous future profits, usually based on some current or political event.

For the cost of your investment and a nominal storage fee, the promoter will purchase the coins and bullion for you and have them

delivered to and stored in a large, well-known bank, nearly always outside of your geographical area. Often, these promoters promise the opportunity to “leverage” your purchase. Leveraging, in theory, is like buying on margin, in that you only make a down payment toward the total cost of the metal you wish to buy. The rest of the money is advanced or loaned to you, with the precious metal serving as collateral. For instance, for \$10,000, you might purchase 22 ounces of gold at \$450 an ounce. By leveraging your purchase at 20 percent down, you could purchase five times as many ounces, or 110 ounces.

The problem with leveraged purchases occurs when the value of this precious metal decreases. As the buyer, you are responsible to cover the downturn in value by putting in more money to cover your 20 percent cash down value. If you fail to cover the downturn, your precious metal is sold (often at a discount), and you are liable for the difference. Leveraging is extremely risky, and not recommended for the casual investor.

Some schemes charge extremely high commissions that must achieve a great increase in the value of coins or metals before you could see a profit. Other schemes do not even bother to purchase the coins or metals. The promoters just take your money and move on to the next town. If you want to purchase precious metals, talk with the local merchants who will deliver the goods to you and who have local reputations to protect.

Agriculture and Livestock

The latest schemes in this area involve ostriches and emus. For a fee, you can invest in a pair of live animals for breeding, with the goal of profiting from the selling of the eggs or offspring to zoos or other ranchers.

Typically, the fee is assessed on a monthly or yearly basis for the board and care of the animals. These investments may be

accompanied by a “buy-back” or repurchase agreement by the promoter, making it appear that the investment is guaranteed against loss.

Remember

To protect yourself from becoming a victim of these or other investment scams, educate yourself before making any investment.